

Service Date: June 23, 1982

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

\* \* \* \* \*

IN THE MATTER of the Application of )  
MOUNTAIN WATER COMPANY for )  
Authority to increase rates and charges )  
for water service in its Missoula, )  
Montana service area. )

UTILITY DIVISION  
DOCKET NO. 81.9.86  
ORDER NO. 4851a

APPEARANCES

FOR THE APPLICANT:

Dennis R. Lopach, Attorney at Law, Hjort & Lopach, P.O. Box 514,  
Helena, Montana 59624

FOR THE INTERVENORS:

John Allen, Staff Attorney, Montana Consumer Counsel, 34 West Sixth  
Avenue, Helena, Montana 59620

FOR THE COMMISSION:

Opal Winebrenner, Staff Attorney, 1227 11th Avenue, Helena, Montana  
59620

BEFORE:

HOWARD L. ELLIS, Commissioner  
JOHN B. DRISCOLL, Commissioner  
THOMAS J. SCHNEIDER, Commissioner

FINDINGS OF FACT

1. On September 30, 1981, Mountain Water Company (Applicant, Mountain or MWC) filed an application with this Commission for authority to increase rates and charges for water service to its customers in Missoula, Montana. The Applicant requested an average increase of approximately 123

percent, constituting a revenue increase of approximately \$2,079,623 in annual revenues.

2. Concurrent with the filing of the permanent application for increased rates, MWC filed an application for an interim increase in rates of approximately 35 percent, equalling an annual revenue increase of \$589,222 or approximately 28 percent of the proposed permanent increase.

3. On October 26, 1981, the Commission having considered the data filed with the Applicant's interim application, issued Order No. 4851 granting the Applicant interim rate relief in the amount of \$589,222 annually.

4. The interim revenue increase was implemented by increasing all metered and flat rates by 49.28 percent, excluding sprinkling water and fire protection service.

5. On March 23, 1982, pursuant to Notice of Public Hearing, a hearing was held in the City Council Chambers, City Hall, Missoula, Montana. For the convenience of the consuming public, an evening session was held March 23, 1982 at 7:00 p.m. in the Missoula County Courthouse, Large Courtroom, to consider the merits of the Applicant's proposed water rate adjustment.

6. At the public hearing, the Applicant presented the testimony and exhibits of:

Daniel M. Conway, Vice President, Revenue Requirements,  
Park Water Company  
Lee Magone, Manager, Mountain Water Company

7. The Montana Consumer Counsel presented the testimony of seven public witnesses at the hearing.

8. The year ending December 31, 1980 test year was uncontested and is found by the Commission to be a reasonable period within which to

measure the Applicant's utility revenues, expenses and returns for the purpose of determining a fair and reasonable level of rates for water service.

#### RATE BASE

9. The Applicant, in its application, proposed an average original cost depreciated rate base of \$7,925,561. In a proposed settlement of issues, entered into between the Applicant and the Montana Consumer Counsel, the Applicant agreed to reduce its working capital, which is a component of rate base, by \$130,000. The Applicant agreed to the adjustment because it had been Commission policy that the cash working capital allowance should reflect the fact that the Applicant has use of accrued property taxes for working capital requirements and this was not reflected in the original rate base proposal. With the above adjustment the Commission finds the original cost depreciated rate base to be \$7,795,561.

#### CAPITAL STRUCTURE

10. The Applicant, in its application, proposed the following capital structure for rate case presentation:

<u>Description</u>	<u>Amount</u>	<u>Ratio</u>
Equity	\$5,559,372	63.11%
Debt	<u>3,250,000</u>	<u>36.89%</u>
Total	\$8,809,372	100.00%

Subsequent to the original filing, and as part of the proposed settlement of issues agreement with the Montana Consumer Counsel, the Applicant reduced its book equity for ratemaking purposes by \$547,339. The Applicant agreed

to reduce its equity by the \$547,339 to reflect the disallowance of an intangible asset as required in this Commission's Order No. 4417b (Montana Power Company, Water Division, General rate increase). The Commission finds that the Equity component in the capital structure should be reduced to \$5,012,033.

11. The Commission accepts the following capital structure for rate case presentation, with qualifications:

<u>Description</u>	<u>Amount</u>	<u>Ratio</u>
Equity	\$5,012,033	60.66%
Debt	<u>3,250,000</u>	<u>39.34%</u>
Total	\$8,262,033	100.00%

12. In accepting the capital structure presented by the Applicant the Commission takes into account that the requested return on equity was reduced from 15 percent to 13.5 percent. The Applicant should be aware that the Commission is unlikely to approve such an "equity rich" capital structure in future rate cases.

The utility industry is extremely capital intensive and leverage is widely used to finance large additions to plant. A debt equity ratio of 60/40 reflects a typical utility capital structure. In addition, a capital structure with a higher proportion of debt is more efficient.

The Commission directs the Applicant to move toward a more normal utility capital structure. Should no change be achieved, it is probable that the Commission will make an explicit adjustment to the capital structure in future rate cases.

COST OF DEBT

13. The debt capital of the Applicant consists of a \$3,250,000 note issued by Park Water Company to Montana Power Company. This debt is an obligation of Park Water Company rather than its subsidiary, MWC, but the note has been properly assigned to the Applicant for ratemaking purposes.

14. The cost of debt or interest on this note is variable, the present cost being 8.80 percent and the cost at maturity being 10.0 percent. The cost of debt presented by the Applicant was not challenged by any party participating in this proceeding and therefore is accepted by the Commission.

COST OF EQUITY

15. The Applicant, in its application, had requested that the Commission allow a return on equity of 15.0 percent. The findings under capital structure indicate that the Applicant is "equity rich." To compensate for this the Applicant has agreed to reduce its requested return on equity from 15.0 percent to 13.5 percent. With this reduction in return on equity, the overall rate of return will more nearly approximate that which would be achieved by the more efficient 60/40 debt equity capital structure.

16. Given the fact that the Applicant has reduced its requested return on equity to 13.5 percent in an effort to more nearly approximate the more efficient capital structure, the Commission finds it appropriate to accept the 13.5 percent return on equity.

CAPITAL STRUCTURE AND COMPOSITE COST OF TOTAL CAPITAL

<u>Description</u>	<u>Amount</u>	<u>Ratio</u>	<u>Cost</u>	<u>Weighted Cost</u>
Equity	\$5,012,033	60.66%	13.5%	8.19%
Debt	<u>3,250,000</u>	<u>39.34%</u>	<u>8.8%</u>	<u>3.46%</u>
Total	\$8,262,033	100.00%		
Composite Cost of Total Capital				11.65%

17. The Commission accepts test year operating revenue of \$1,688,574.

OPERATING EXPENSES

18. The Applicant, in its application, proposed pro forma adjustments increasing operation and maintenance by \$117,424.

19. Consistent with the proposed settlement of issues, entered into by the Applicant and the Consumer Counsel, the Applicant reduced the \$117,424 by \$12,776 to reflect a non-recurring expense item, which was a charge from Montana Power Company for services performed prior to the Applicant's Missoula office becoming operational.

20. The Commission accepts pro forma adjustments increasing operation and maintenance expense by \$104,648 and finds operation and maintenance expense under present rates to be \$1,452,690.

21. The Applicant originally proposed that "Taxes Other than Income" be at the level of \$305,798. These taxes were reduced by \$24,735 with the substitution of the actual 1981 property tax instead of utilizing the Applicant's projection. The Commission finds "Taxes Other than Income" to be \$281,063.

22. The Applicant proposed depreciation expense of \$227,657. This expense was not challenged by any party participating in this proceeding and therefore is accepted by the Commission.

REVENUE REQUIREMENT

23. Based on the preceding Findings of Fact, the Commission finds that in order to produce a rate of return of 11.65 percent on MWC average original cost depreciated rate base, the Applicant will require additional annual revenues in the amount of \$1,870,307 from its Missoula, Montana water utility.

24. Applicant's accepted test year pro forma operating revenues, expenses and rate of return are summarized as follows:

## MOUNTAIN WATER COMPANY - MISSOULA DIVISION

	Company Pro Forma (Present Rate)	Adjustments	Adjusted	To Eliminate Negative Taxes	To Produce 11.65 Rate of Return	Accepted by the Commission
Operating Revenues	\$1,688,574	-0-	\$1,688,574	\$ 471,766	\$1,398,541	\$3,558,881
Operating Revenue Deductions						
Operating Expenses	\$1,465,466	(12,776)	\$1,452,690			\$1,452,690
Depreciation	227,657	-0-	227,657			227,657
Taxes Other Than Income	305,798	(24,735)	281,063	425	1,259	282,747
Federal Income Tax (Net ITC)	(219,515)	17,333	(202,182)	202,182	594,643	594,643
State Income Tax	(35,705)	2,533	(33,172)	31,816	94,317	92,961
Total Deductions	\$1,743,701	(17,645)	1,726,056	234,423	690,219	2,650,698
Operating Income	(55,127)		(37,482)	237,343	708,322	908,183
Rate Base (OC-D)	\$7,925,561	(130,000)	7,795,561			7,795,561
Rate of Return (OC-D)	(0.70)		(0.48)			11.65



ALLOCATED COST OF SERVICE

25. The Applicant in its filing presented an allocated cost of service study which determined the cost of providing water service to the various customer classifications. The Commission accepts the premises utilized by the Applicant in determining the cost of providing service to the various customer classifications, and therefore finds the cost of service study fairly presents the Applicant's cost of providing water service to the various customer classifications.

DERIVATION OF INCREASED RATES

26. The Commission accepts the methodology employed by the Applicant for determination of increased rates applicable to each customer classification with the exception of metered water service.

27. The Applicant in determining the applicable rate for metered water service assigned two-thirds of its fixed cost of providing water service to the service charge component of the rate structure. On cross-examination the Applicant stated that the assignment of two-thirds of the fixed cost to a service charge was subjective and that his reasoning for doing so was to minimize the effect water conservation and customer resistance to rate increases would have on the consumption charge in future proceedings, and to provide greater revenue stability for the Company.

The Commission recognizes that the assignment of two-thirds of the fixed costs to a service charge will result in the Applicant having a greater revenue stability but rejects this assignment because part of the expenses assigned to service are properly a function of consumption. Therefore, the Commission will substitute its judgment for assignment of fixed costs to

service for that of the Applicant. The Commission finds that it would be appropriate to assign one-third of the fixed costs to the service charge component of the rate structure and the balance to the consumption charge.

MODIFICATION OF RULES

28. The Applicant proposed the elimination of the following sentence from Special Term and Condition 6 of the Flat Rate Water Service Schedule and from Special Term and Condition 3 of the Sprinkling Water Service Schedule:

Any consumer has the privilege of paying for water by meter measurement under the regular rules and rates, the meter being furnished and maintained by the Water Company.

The Commission in its Rules Governing Water Service Provided by Privately-Owned Water Utilities has provided that any consumer may have a meter placed by the utility. The Commission can find no reason why it should deviate from its general rules and therefore denies the Applicant's request to eliminate the above sentence from its Special Terms and Conditions.

29. By denial of elimination of the sentence in Finding of Fact No. 28, the Commission cannot allow the modification of Rule 9-1 of the Company's Service Regulations.

30. The Applicant has requested that the Company be allowed to prohibit consumers having metered water service from availing themselves of flat rate sprinkling water. The Commission finds the prohibition against metered customers utilizing the flat rate for sprinkling purposes to be appropriate.

31. The Applicant has also requested that they be allowed to discontinue the "Budget Billing Plan" for sprinkling water. The Commission is of the opinion that consumers should have the option of budget billing so that they may equalize their water utility bills. The Applicant's request to eliminate the budget billing plan is denied.

CONCLUSIONS OF LAW

1. The Montana Public Service Commission properly exercises jurisdiction over the parties and subject matter in this proceeding. Section 69-3-102, MCA.

2. The Commission afforded all parties interested in this proceeding proper notice and an opportunity to participate. Section 69-3-303, MCA.

3. The rates approved herein are reasonable, just and proper. Section 69-3-201, MCA.

ORDER

NOW THEREFORE, at a session of the Montana Public Service Commission, Department of Public Service Regulation, held in its offices at 1227 11th Avenue, Helena, Montana 59620, on this 21st day of June, 1982, there being present a quorum of Commissioners, there came regularly before the Commission for final action the matters and things in Docket No. 81.9.86, and the Commission being fully advised in the premises;

IT IS ORDERED by the Commission that Mountain Water Company shall file rate schedules which reflect an increase in annual revenues of \$1,870,307 for its Missoula, Montana service. These revenues are in lieu of and not in addition to the revenues granted in this Commission's Order No. 4851.

IT IS FURTHER ORDERED that the water revenues authorized herein shall be distributed among the Applicant's clases of service as provided herein.

IT IS FURTHER ORDERED that the Applicant may modify its rules and regulations as provided herein, and shall provide a copy of the modification to the Commission.

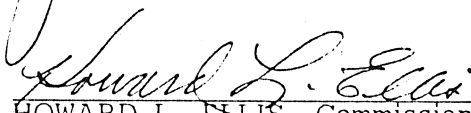
IT IS FURTHER ORDERED that the rates shall not be effective until approved by the Commission.

IT IS FURTHER ORDERED that a full true and correct copy of this order be sent forthwith by first class United States mail to the Applicant and to all other appearances herein.

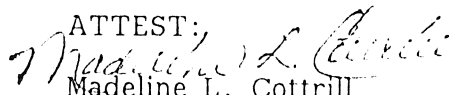
THE FOREGOING ORDER was adopted by the Department of Public Service Regulation of the State of Montana, Public Service Commission, IN OPEN SESSION at Helena, Montana, this 21st day of June, 1982, by a vote of 3 - 0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

  
JOHN B. DRISCOLL, Commissioner

  
HOWARD L. ELLIS, Commissioner

  
THOMAS J. SCHNEIDER, Commissioner

ATTEST:  
  
Madeline L. Cottrill  
Secretary

(SEAL)

NOTE: You may be entitled to judicial review of the final decision in this matter. If no Motion for Reconsideration is filed, judicial review may be obtained by filing a petition for review within thirty (30) days from the service of this order. If a Motion for Reconsideration is filed, a Commission order is final for purpose of appeal upon the entry of a ruling on that motion, or upon the passage of ten (10) days following the filing of that motion. cf. the Montana Administrative Procedure Act, esp. Sec. 2-4-702, MCA; and Commission Rules of Practice and Procedure, esp. 38.2.4806, ARM.